

January 24, 2014

Ryan Hodge, Assistant City Attorney
Office of the City Attorney
20 Civic Center Plaza, P.O. Box 1988
Santa Ana, California 92702

Re: Your Request for Advice
Our File No. C-14-012

Dear Mr. Hodge:

This letter responds to your request for advice regarding the conflicts-of-interest provisions under Government Code section 1090 et seq.¹ Because the Fair Political Practices Commission (“the Commission”) does not act as a finder of fact when it renders assistance (*In re Oglesby* (1975) 1 FPPC Ops. 71), this letter is based on the facts presented.

Please note that after forwarding your request to the Attorney General’s Office and the Santa Ana District Attorney’s Office, we did not receive a written response from either entity. (See Section 1097.1(c)(4).) Finally, we are required to advise you that the following advice is not admissible in a criminal proceeding against any individual other than the requestor. (See Section 1097.1(c)(5).)

QUESTION

Does the exception to Section 1090 for “public services generally provided” permit a Santa Ana City Councilmember to enter into a Mills Act² contract with the City of Santa Ana?

CONCLUSION

No. The exception to Section 1090 for “public services generally provided” does not permit a Santa Ana City Councilmember to enter into a Mills Act contract with the City of Santa Ana.

¹ All further statutory references are to the Government Code, unless otherwise indicated.

² The Mills Act is located in Section 50280 et seq.

FACTS

In 1972, California legislators adopted the Mills Act, which authorizes local governments to enter into a contract with the owner of a qualified historical property who agrees to rehabilitate, restore, preserve, and maintain the property in exchange for property tax reductions. The amount of tax savings varies, but Mills Act Agreements authorize up to 50 percent property tax savings.³

The City of Santa Ana is a local government participant in the program and enters into Mills Act Agreements with qualified historical property owners. An owner of a qualified historical property who wants to participate in the Mills Act Program must submit an application to the City of Santa Ana, which is then reviewed and must be approved by the City of Santa Ana Historic Resources Commission and City Council. An approved application results in the formation of a Historic Property Preservation Agreement, which remains in effect for a minimum of ten years. The types of preservation conditions established by the Mills Act Agreement are different for each property's specific needs,⁴ but all contracts must contain certain statutorily specified terms.

A current member of the Santa Ana City Council owns a historical property which may qualify for participation in the City's Mills Act program, entitling the councilmember to receive property tax credits. However, according to your letter, there is concern that receipt of a tax credit would violate Section 1090, as the tax credit is a financial interest created through a Historic Preservation Agreement, which is required to be approved by the City Council.

ANALYSIS

Section 1090 generally prohibits public officers, while acting in their official capacities, from making contracts in which they are financially interested. Section 1090 is concerned with financial interests, other than remote or minimal interests, that prevent public officials from exercising absolute loyalty and undivided allegiance in furthering the best interests of their agencies. (*Stigall v. Taft* (1962) 58 Cal.2d 565, 569.) Section 1090 is intended “not only to strike at actual impropriety, but also to strike at the appearance of impropriety.” (*City of Imperial Beach v. Bailey* (1980) 103 Cal.App.3d 191, 197.)

Under Section 1090, “the prohibited act is the making of a contract in which the official has a financial interest.” (*People v. Honig* (1996) 48 Cal.App.4th 289, 333.) A contract that violates Section 1090 is void. (*Thomson v. Call* (1985) 38 Cal.3d 633, 646.) The prohibition applies regardless of whether the terms of the contract are fair and equitable to all parties. (*Id.* at pp. 646-649.)

³ See http://www.ci.santa-ana.ca.us/pba/planning/Historic_Preservation_Incentives.asp

⁴ *Ibid.*

We employ the following six-step analysis to determine whether the Santa Ana City Councilmember has a disqualifying conflict of interest under Section 1090.

Step One: Is the City Councilmember subject to the provisions of Section 1090?

Section 1090 provides, in part, that “[m]embers of the Legislature, state, county, district, judicial district, and city officers or employees shall not be financially interested in any contract made by them in their official capacity, or by any body or board of which they are members.” City councils and their members are plainly covered by this prohibition. (See, e.g., *Thomson, supra*, at p. 645; *City Council v. McKinley* (1978) 80 Cal.App.3d 204, 213.)

Step Two: Does the decision at issue involve a contract?

To determine whether a contract is involved in the decision, one may look to general principles of contract law (84 Ops.Cal.Atty.Gen. 34, 36 (2001);⁵ 78 Ops.Cal.Atty.Gen. 230, 234 (1995)), while keeping in mind that “specific rules applicable to Sections 1090 and 1097 require that we view the transactions in a broad manner and avoid narrow and technical definitions of ‘contract.’” (*People v. Honig, supra*, at p. 351 citing *Stigall, supra*, at pp. 569, 571.)

Here, the decision at issue necessarily involves a contract because under the Mills Act, the councilmember must enter into a contract with the City of Santa Ana in order to participate in the program and receive the property tax credits for the historical property.

Step Three: Is the councilmember making or participating in making a contract?

As a member of the Santa Ana City Council, which ultimately must approve any agreement under the Mills Act, the councilmember would be participating in the making of a contract.

Step Four: Does the councilmember have a financial interest in the contract?

Under Section 1090, “the prohibited act is the making of a contract in which the official has a financial interest” (*People v. Honig, supra*, at p. 333), and officials are deemed to have a financial interest in a contract if they might profit from it in any way. (*Ibid.*) Although Section 1090 nowhere specifically defines the term “financial interest,” case law and Attorney General opinions state that prohibited financial interests may be indirect as well as direct, and may involve financial losses, or the possibility of losses, as well as the prospect of pecuniary gain. (*Thomson, supra*, at pp. 645, 651-652; see also *People v. Vallergera* (1977) 67 Cal.App.3d 847, 867, fn. 5; *Terry v. Bender* (1956) 143 Cal.App.2d 198, 207-208; *People v. Darby* (1952) 114

⁵ It is noteworthy to point out that opinions issued by the Attorney General’s Office are entitled to considerable weight (*California Assn. of Psychology Providers v. Rank* (1990) 51 Cal.3d 1, 17), especially where, as here, it has regularly provided advice concerning a particular area of law. (*Thorpe v. Long Beach Community College Dist.*, (2000) 83 Cal.App.4th 655, 662; *Freedom Newspapers, Inc. v. Orange County Employees Retirement System* (1993) 6 Cal.4th 821, 829.)

Cal.App.2d 412, 431-432; 85 Ops.Cal.Atty.Gen. 34, 36-38 (2002); 84 Ops.Cal.Atty.Gen. 158, 161-162 (2001).)

In the present situation, the councilmember would have a plain financial interest in the Mills Act contract based on his or her resulting entitlement to receive property tax credits. As stated, the amount of the tax credit varies, but a Mills Act Agreement allows for up to 50 percent tax savings.

Step Five: Does either a remote interest or non-interest exception apply?

As a general rule, when Section 1090 is applicable to one member of a governing body of a public entity, as here, the prohibition cannot be avoided by having the interested board member abstain; the entire governing body is precluded from entering into the contract. (*Thomson, supra*, at pp. 647-649; *Stigall, supra*, at p. 569; 86 Ops.Cal.Atty.Gen. 138, 139 (2003); 70 Ops.Cal.Atty.Gen. 45, 48 (1987).) However, the Legislature has created various statutory exceptions to Section 1090's prohibition where the financial interest involved is deemed to be a "remote interest," as defined in Section 1091, or a "noninterest," as defined in Section 1091.5.

If a "remote interest" is present, the contract may be made if (1) the officer in question discloses his or her financial interest in the contract to the public agency, (2) such interest is noted in the entity's official records, and (3) the officer abstains from any participation in the making of the contract. (Section 1091(a); 88 Ops.Cal.Atty.Gen. 106, 108 (2005); 83 Ops.Cal.Atty.Gen. 246, 248 (2000).) If a "noninterest" is present, the contract may be made without the officer's abstention, and generally a noninterest does not require disclosure. (*City of Vernon v. Central Basin Mun. Water Dist.* (1999) 69 Cal.App.4th 508, 514-515; 84 Ops.Cal.Atty.Gen. 158, 159-160 (2001).)

As your letter points out, the one exception that merits discussion is the "noninterest" specified in Section 1091.5(a)(3), which provides that an officer or employee shall not be deemed to be interested in a contract if his or her interest is "[t]hat of a recipient of public services generally provided by the public body or board of which he or she is a member, on the same terms and conditions as if he or she were not a member of the body or board."

The issue here distills to whether the property tax credits available pursuant to the Mills Act program are considered "public services generally provided" under Section 1091.5(a)(3). It has been stated that "[t]he phrase 'public services generally provided' is not self-defining, nor is there any useful legislative history that might shed light on the Legislature's intent." (*Lexin v. Superior Court* (2010) 47 Cal.4th 1050, 1086.) However, Attorney General opinions and case law make clear that the exception is intended to apply only to services that are uniformly provided to all customers and for which rates and charges have been clearly established, such as public utilities (water, gas, and electricity), and the renting of hangar space in a municipal airport on a first come, first served basis. (See e.g., 81 Ops.Cal.Atty.Gen. at p. 319; *City of Vernon, supra*, at p. 516.)

In contrast, where administering officials are required to exercise judgment or discretion, the exception has been found not to apply. For example, a prior Attorney General opinion considered whether Section 1090 barred a city councilman from participating in a city-sponsored loan program for developing businesses within the city. (81 Ops.Cal.Atty.Gen. at p. 317.) When confronting whether this program constituted a “public service” under Section 1091.5(a)(3), the opinion noted that unlike services for public utilities, acquiring a government loan involved more complex considerations as the “loan applicant must qualify, and the public official approving the loan must exercise some degree of discretion and judgment.” (81 Ops.Cal.Atty.Gen. at p. 319.) It further stated, “[w]hatever may be the scope of the ‘public services’ exemption of Section 1091.5, subdivision (a)(3), it does not include the extension of a business development loan, where the conditions of the loan would be specific to the particular proposal in question.” (*Ibid.*)

In another opinion, a member of a County Air Pollution Control District’s Board of Directors wanted to participate in the county’s grant funding program, which provided funds to entities and individuals for the purchase or retrofit of certain engines and equipment. (92 Ops.Cal.Atty.Gen. 67 (2009).) In order to qualify, it was necessary to submit an application to the district, which the district then reviewed “to determine whether it meets all eligibility requirements set forth in the Health and Safety Code, the 2005 Guidelines, and the district’s own policies and procedures.” (92 Ops.Cal.Atty.Gen. at p. 68.)

The opinion examined previous situations where the “public service” exemption had been recognized concluding that the services in those instances were “provided without any exercise of judgment and discretion by the public officials involved. It is the absence of judgment and discretion that distinguishes these examples from the grant-award process under discussion here.” (92 Ops.Cal.Atty.Gen. at p. 70.) The opinion continued by stating:

It is true that because limited funds are available, grants under the Carl Moyer program are available to a relatively small number of applicants. However, that factor alone would not necessarily cause us to rule out a public services exception. “Public agencies provide many kinds of ‘public services’ that only a limited portion of the public needs or can use. This does not derogate from their characterization as ‘public services’ according to the ordinary meaning of those words.” (*City of Vernon, supra*, at p. 515.) Additionally, we are informed that the board considers applications on a first come, first served basis, which gives them at least some surface indicia of being administered objectively and without favor. On balance, though, we conclude that the Carl Moyer program simply does not contemplate that grants will be awarded on the “same terms and conditions” to all applicants, as is required by Section 1091.5(a)(3). A grant is to be awarded only after an application has been individually scrutinized and evaluated to determine its compliance with statutory criteria. Each application is weighed according to the characteristics of the proposed engine, its emissions performance, its cost-effectiveness (i.e., emissions reduction per dollar of cost), and considerations of whether the engine is cleaner than required under the applicable air quality

laws have been ascertained. The district's evaluation may also include a determination “that an application is not in good faith, not credible, or not in compliance with [the governing statute] and its objectives.” These considerations require the exercise of judgment and discretion.

The “public services generally provided” exemption of Section 1091.5(a)(3) does not, in our view, encompass the awarding of a grant that must be based upon consideration of conditions unique to each proposal and subject to the particularized judgment and discretion of the district or its board. Although we recognize that the goals of the Carl Moyer Program are advanced by making its grants available to otherwise qualified applicants, to permit them to be awarded to members of the board would be contrary to long-established policy and authority on conflicts of interest.

(92 Ops.Cal.Atty.Gen. at p. 70.)⁶

It is clear that the present matter does not concern services such as the provision of public utilities that have predetermined rates uniformly provided to all customers without the need to exercise discretion and judgment. Instead, the property tax savings program here is similar to the loan and grant funding programs described above in that the administering officials from the City of Santa Ana will be required to exercise judgment and discretion not only in negotiating the terms of each contract under the Mills Act, but also in the continued enforcement of those terms. The Mills Act appears to allow local governments and qualified owners to negotiate certain specific terms of the contract. Indeed, the City of Santa Ana’s website states “[t]he types of preservation conditions established by the Mills Act Agreement are different for each property's specific needs.”⁷ Further, the contract must be reviewed and approved by City of Santa Ana Historic Resources Commission and the City Council.

The Mills Act requires a minimum 10-year term with automatic yearly extensions. (Sections 50281(a) & 50282(a).) Moreover, it requires that each contract provide for periodic inspections by the appropriate government officials to determine the owner’s compliance with the terms of the contract. (Sections 50281(b)(2) & 50282(a).) The Mills Act also provides discretion to the administering officials to elect *not* to renew the contract for any reason. (Section 50282.) Finally, the administering officials have the authority to impose penalties if they determine the owner has breached the contract or failed to adequately protect the historic property. (Section 50284.)

In our view, from the initial review and approval of the application and contract to the ongoing contract compliance and renewal decisions, the Mills Act requires government officials to exercise discretion and judgment similar to the loan and grant programs described above. For this reason, we do not believe a contract under the Mills Act falls within the scope of the “public

⁶ All references to footnotes within the quoted text were removed.

⁷ See http://www.ci.santa-ana.ca.us/pba/planning/Historic_Preservation_Incentives.asp.

services generally provided” exemption of Section 1091.5(a)(3), and the councilmember would violate Section 1090 by entering into such a contract with the City of Santa Ana.

Step Six: Does the rule of necessity apply?

In limited circumstances, a “rule of necessity” has been applied to allow the making of a contract that Section 1090 would otherwise prohibit. (88 Ops.Cal.Atty.Gen. 106, 110 (2005).) Under the rule of necessity, a government agency may acquire an essential service, despite the existence of a conflict, when no source other than that which triggers the contract is available; the rule “ensures that essential government functions are performed even where a conflict of interest exists.” (*Eldridge v. Sierra View Hospital Dist.* (1990) 224 Cal. App. 3d 311, 322.)

You have provided no facts to suggest the “rule of necessity” would apply in the present situation.

If you have other questions on this matter, please contact me at (916) 322-5660.

Sincerely,

Zackery P. Morazzini
General Counsel

By: Jack Woodside
Senior Counsel, Legal Division

JW:jgl